Introduction

Homeowners Multi Peril Insurance

Fire insurance on real property has been commonplace in the United States since the nineteenth century. The 1950's saw the introduction of the homeowners multi-peril insurance policy which provided a more comprehensive coverage for damage from fire and additional perils as well as coverage for personal liability arising from use of the real property. These homeowner multi peril insurance policies became the standard by the 1960's with Insurance Services Office, Inc. (ISO), an industry rating and statistical organization, as the lead sponsor of the standard homeowners insurance policies since that time.[2]

FAIR Plans

In the 1960's the United States experienced a period of civil unrest. This unrest resulted in extensive property damage (not to mention loss of life) in a number of large metropolitan areas across the entire United States. This led to a significant change in the insurance and reinsurance markets as it related to the protection of urban property. A national advisory panel on the nation's cities advised the President of the United States that fair access to property insurance was a prerequisite for revitalization of urban America. Following the recommendation of the advisory panel, Congress enacted the Urban Property and Reinsurance Act of 1968. This Act authorized the establishment of "FAIR (Fair Access to Insurance Requirements) Plans" along with federal riot reinsurance to insurers.

Massachusetts followed this federal legislation with Chapter 731 of the Acts of 1968 which established the Massachusetts FAIR Plan formally known as the Massachusetts Property Insurance Underwriting Association (MPIUA). The urban areas of operation[3] for the MPIUA were initially determined by the Commissioner of Insurance to be one county and a number of Massachusetts cities.[4] The MPIUA offered coverage on both a personal and commercial lines basis. On the personal lines side it offered a standard fire insurance policy, insurance against direct loss from the perils of vandalism and malicious mischief, along with extended coverage to homeowners in these urban areas of the commonwealth. The MPIUA operated similar to an insurance company in inspecting property, collecting premium, issuing its own policies, and adjusting its own claims.

In 1970 the Commissioner of Insurance promulgated 211 CMR 5.00. This regulation broadened the definition of urban area to include the entire Commonwealth of Massachusetts. It also established the commission rate to brokers placing business in the

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[2] General revisions of these homeowners policies have historically been filed by ISO on an intermittent basis, usually once every five to ten years.

[3] Chapter 731 of the Acts of 1968 defined urban area as "any city or town, or streets or sections thereof, in the commonwealth so designated by the commissioner after appropriate hearing." This designation was subsequently accomplished through regulation, 211 CMR 5.00.

[4] The County of Suffolk and the cities of Brockton, Cambridge, Fall River, Haverhill, Lawrence, Lowell, Lynn, New Bedford, Somerville, Springfield and Worcester.

MPIUA at 12% of the premium charged to the insured.[5] This was followed in 1975 by the promulgation of 211 CMR 21.00. This regulation broadened the personal lines coverage offered by the MPIUA from the standard fire insurance policy and extended coverage to the homeowners multi peril insurance policy. In addition, it tied the premium rates charged to homeowners by the MPIUA to the published manual rates of the ISO for standard homeowners risks.[6] Both regulations were found to be inconsistent with Chapter 93 of the Acts of 1996 and were subsequently repealed.

Studies of Urban Insurance Availability (Redlining)

The issue known as "redlining" or unfair discrimination against a risk solely due to geographic location and/or racial or ethnic characteristics of the insured has been a controversial issue in property insurance since at least the 1960's and remains so to this day.

Charges of redlining have been raised from time to time against specific property insurers and the property insurance industry as a whole over the years. In 1993-95 the National Association of Insurance Commissioners (NAIC)[7] undertook several studies on the issues of availability and affordability of urban insurance in the personal automobile and homeowners insurance markets.[8]

The results of the NAIC studies were not conclusive one way or another regarding the confirmation or rejection of the contentions regarding homeowners insurance redlining in urban areas. However, these studies did point out that there were insurance availability problems in many urban areas. The exact cause(s) of the lack of insurance availability was not determined. A number of different causes were proposed including underwriting practices, lack of producer outlets, rate inadequacy, and insurer misconceptions relative to urban risks. In addition, nationally premiums were found to be generally higher in urban areas, but so were the loss costs (cost of claims) associated with that business.

In 1995 following the release of the NAIC studies the Massachusetts Division of Insurance (DOI) through its Special Investigative Unit (SIU) conducted an examination of eight insurers who were major writers of coverage in the Massachusetts homeowners insurance market and representative of the market as a whole.[9] The SIU examination focused on the marketing and underwriting practices of these insurers in the Boston area. The purpose of the examination was to determine whether any of the eight insurers were

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[5] The 12% commission rate has remained constant since that time.

[6] The ISO rates were based on premium and loss data from all insurance companies that reported their premium and loss data to ISO as their statistical agent. These insurers at that time collectively wrote more than 70% of the homeowners insurance market in Massachusetts.

[7] This association of state insurance commissioners was formed for the purposes of gathering and exchanging information relative to insurance as well as the development of uniformity and consistency of individual state regulation through model laws and regulations.

[8] *A Preliminary Analysis of Urban Insurance Markets*, Robert W. Klein, 1994. *Urban Insurance Problems And Solutions: Interim Report*, National Association of Insurance Commissioners Insurance Availability and Affordability (EX3) Task Force, 1994. *The Impact of Loss Costs on Urban Homeowners Insurance Markets*, Robert W. Klein, 1995.

[9] *Report of Examination of Homeowner Insurance Availability in The Metropolitan Boston Area*, Massachusetts Division of Insurance, November 1995.

engaged in illegal discriminatory underwriting in Boston or any of its neighborhoods. This examination did not reveal any illegal discrimination by these insurers.

While the NAIC studies were not definitive, they did help focus attention on the need for insurers to reassess their approach to urban markets. In Massachusetts this resulted in at least two small changes. First, a brokerage system[10] was designed to help insurers find potential customers who met their underwriting criteria. Second, a cooperative effort between the Massachusetts Affordable Housing Alliance (MAHA) and several insurers was undertaken to encourage risk management training for insureds, with discounted premiums as the immediate reward.

Chapter 93 of The Acts of 1996

A consensus for reform in the Massachusetts homeowners insurance market had been building during and following the NAIC studies and the subsequent DOI examination. All the participants involved in the market, insurers, insurance agents, consumers, legislators, and regulators, realized that something had to be done to address the issues of voluntary market[11] homeowners insurance availability in urban and coastal areas.

All segments of the market provided input to the proposed legislation that was intended to resolve the issue of both urban and coastal homeowners insurance availability. However, there were a number of fundamental requirements if this legislation were to be successful in alleviating the voluntary market availability problems. These fundamental requirements included monetary incentives for insurers to write urban and coastal property in the voluntary market, a change in the way that FAIR Plan (MPIUA) rates were determined, and most importantly regular reporting so that analysis of comprehensive homeowners insurance data on both an individual company and industry basis could occur.

On May 20, 1996, Chapter 93 of the Acts of 1996, An Act Relative to Insurance Redlining, was signed into law by Governor Weld. This legislation took effect immediately.[12] Some of the major points of this legislation included the following:

1. Provided MPIUA assessment credits in 1997-98 for insurers writing voluntary business in territories where the MPIUA had high market penetration.

2. Required MPIUA to provide assessment credits starting January 1, 1999 for insurers writing voluntary business in zip codes where the MPIUA had high market penetration.

The following MPIUA proposed calendar year credit eligible zip codes were approved for 2003 for writing credits along with their respective weights:

Zip Code	*Town*	*Weight*
02119	*(Boston-Roxbury)*	*1.0*
02121	*(Boston-Dorchester)*	*1.0*

[10] This market assistance plan (MAP) was required by Chapter 93 of the Acts of 1996.
[11] The voluntary market does not include Excess or Surplus Lines.
[12] Chapter 93 of the Acts of 1996 had an emergency preamble that made the statute effective on enactment.

02047 (Scituate-Humarock)	*1.0*
02125 (Boston-Dorchester)	*.90*
02128 (Boston–East Boston)	*.90*
01841 (Lawrence)	*.80*
02126 (Boston-Mattapan)	*.70*
02150 (Chelsea)	*.70*
02124 (Boston-Dorchester)	*.70*
02065 (Marshfield-Ocean Bluff)	*.70*
02120 (Boston-Roxbury Crossing)	*.70*
02122 (Boston-Dorchester)	*.60*

3. Provided MPIUA assessment credits for insurers writing voluntary business in coastal territories where more than 60% of the territory business had previously been written in the MPIUA ("take-out credits"*)*.

4. Required MPIUA to provide take-out credits starting January 1, 1999 for insurers writing voluntary business in coastal zip codes where the MPIUA had a greater than 60% market penetration.

No zip codes were eligible for take out credit for calendar year 2003.

5. Tied MPIUA rate changes to rate changes in the voluntary market.

MPIUA Rate Changes Since 1996 Reform Law

Effective Date	Overall Rate Change
12/31/96	+5.30%
12/31/97	+2.23%
12/31/98	+0.92%
12/31/99	+0.13%
12/31/00	-0.51%
12/31/01	-0.17%
12/31/02	+1.92%
12/31/03	+2.80%

MPIUA submitted its eighth homeowners insurance rate filing under this law on August 28, 2003 with a stipulated overall increase of +2.80% to be effective December 31, 2003. A public hearing on this proposal was held on November 4, 2003. The parties to this hearing (MPIUA, State Rating Bureau, and Attorney General) reached a stipulated agreement. The Commissioner of Insurance approved the stipulation on November 25, 2003 effectively accepting the proposal as submitted.

6. Provided for the top twenty-five insurers and the MPIUA to annually provide detailed cancellation and non-renewal information by zip code for homeowners insurance.

This is the ninth consecutive year this type of data has been provided. (See Appendix A)

7. Provided for all statistical agents for homeowners insurance in Massachusetts to submit detailed premium and loss data by territory by form, aggregate insurer premium and loss data by cause of loss by territory by form and by designated zip code by form on an individual company basis.[13]

8. Provided that the Commissioner of Insurance report annually on the state of the Massachusetts homeowners insurance market after substantial analysis of the data submitted in (6) and (7). (Note: "homeowners insurance" has several forms, but the general touchstone is that the insured is the occupant. Real and personal property may be covered as well as personal liability.)

This report is the ninth such annual report.

9. Authorized alternative loss settlement practices subject to the use of disclosure forms designed by the Commissioner.

The Division in 1998 placed on file ISO Actual Cash Value/Functional Replacement Cost loss settlement options for homeowners and dwelling fire insurance policies. These options became effective March 1, 1999 and are available on forms 02 & 03.

10. Required the MPIUA to offer an installment plan and provide coverage for scheduled personal property.

MPIUA implemented its Premium Installment Payment Program effective October 15, 1997. The program requires a 25% down payment with three equal installment payments.

MPIUA Scheduled Personal Property Coverage was made available effective September 1, 1997. MPIUA's program and rates for this coverage are consistent with and similar to the programs and rates utilized by insurers in the Massachusetts voluntary market.

11. Required the MPIUA to develop a market assistance plan (MAP) to assist applicants to obtain homeowners insurance in the voluntary market.

MPIUA implemented its initial Massachusetts Market Assistance Plan (MA-MAP) effective October 15, 1997. A review of MA-MAP statistics for the first two years of operation show that more than 90% of insureds whose policies were referred to the MA-MAP and were offered policies in the voluntary market declined such offers.[14] As a result the initial MA-MAP was revised effective July 1, 1999, so that every qualifying MPIUA homeowners insured[15] is given the option of participating in the MA-MAP. At

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[13] The first data submission provided in 1996 was exclusively on a territorial basis. All subsequent data submissions have been required to include certain data on a zip code basis.

[14] *1999 Report on the Current State of The Homeowners Insurance Market in The Commonwealth*, Exhibit 21, page 2.

[15] Under the original MA-MAP every qualifying new business owners form applicant was automatically submitted to the MA-MAP.

present nine (9) insurers are participating in MA-MAP. The following revisions to MA-MAP were approved by the Commissioner effective July 1, 1999:

1. All qualifying new business and renewal applications for coverage with MPIUA will be sent to participating insurers on the request of the applicant; and
2. Applicants with two or more losses during the prior 24 months will not be eligible. Additionally, applicants against whom a dog bite claim, not involving trespass, has been filed are not eligible.

General principles of the MA-MAP also include a 15% commission level to participating broker/agents and the provision to each participating insurer of a quarterly list of FAIR Plan properties that have been "loss free" for five years or more.

Annual Reports

The Commissioner issued her first annual report in October 1996, *Report on the Current State of the Massachusetts Homeowners Insurance Market Pursuant to the Authority and Direction of Chapter 93 of the Acts of 1996*. This report reviewed Massachusetts homeowners insurance data for the calendar years 1994-1995. The statistical agents were required to provide premium and loss experience by individual insurance company by standard ISO rating territories for all companies that had written homeowners insurance business in 1994 and 1995. The top twenty-five insurers were required to provide by designated zip code the number of policies in force, the number of cancellations, and the number of non-renewals for calendar years 1994 and 1995.

The Commissioner issued her second annual report in October 1997 based upon Massachusetts homeowners insurance data for calendar year 1996. The statistical agents were required to provide one additional data element, premium and loss experience by individual insurance company by designated zip codes for the top twenty-five insurers by 1996 written premium.[16] The Commissioner issued her third annual report in December 1998 based upon Massachusetts homeowners insurance data for calendar year 1997. The statistical agents were required to provide another additional data element, written premium data by all Massachusetts zip codes for the top twenty-five insurers by 1997 written premium. [17]

Ninth Annual Report

This year's report reviews Massachusetts homeowners insurance data for calendar year 2003. The statistical agents were required to provide for all reporting insurers voluntary aggregate 2001, 2002 and 2003 written premium data by all Massachusetts zip codes and by ISO Massachusetts homeowners insurance territories. ISO, as the current statistical agent for the FAIR Plan, would provide corresponding data for the FAIR Plan. The statistical agents were also required to provide premium and loss experience for each of their reporting companies writing in Massachusetts in 2003 by individual insurance company by standard ISO rating territories, similar data by designated zip codes for the top twenty-five insurers by 2003 written premium, and aggregate 2003 data by cause of

[16] This statutory requirement was required for the 1997 and subsequent reports.
[17] This statutory requirement was required for the 1998 and subsequent reports.

loss by territory by form for all reporting insurers and separately for the FAIR Plan. The top twenty-five insurers were required to provide by designated zip code the number of policies in force, the number of cancellations, and the number of non-renewals for calendar year 2003.

Despite the Commissioner's efforts to check data for accuracy, she is ultimately dependent upon the rating organizations' and companies' accuracy in providing complete and accurate data.

Analysis of Premium and Loss Experience

2003 Loss Ratio Experience

The loss ratio (incurred losses divided by earned premium) is one generally accepted measure of the underwriting success or failure of property insurance. The 2003 overall loss ratio inclusive of loss adjustment expense for the total Massachusetts homeowners insurance market based upon the submitted loss data was 59.4%. This loss ratio is indicative of a good year from an underwriting perspective.[18] The corresponding loss ratios for 1994, 1995, 1996, 1997, 1998, 1999, 2000, 2001 and 2002 were 67.9%, 48.4%, 87.2%, 49.6%, 45.8%, 46.9%, 55.1%, 56.6% and 51.1% respectively. These loss ratios indicate that 1995, 1997, 1998, 1999, 2000, 2001 and 2002 were also good years from an underwriting perspective. This again confirms the general principle that success or failure of homeowners insurance in an overall market sense is significantly dependent upon the weather (see Exhibit 16) and catastrophic events. 2003 saw an increase for Massachusetts in terms of snowfall and one catastrophe. The non-weather related causes of loss generate fewer sharp increases/decreases in losses[19] and claims from year to year, whereas the weather related causes of loss often show more significant fluctuations from year to year (Exhibit 12).

The total market overall loss ratio for 2003 of 59.4% can be further broken down into 2003 loss ratios by homeowners type of policy form. This breakdown is as follows:

Form	Loss Ratio
Condominium	.484
Dwelling	.610
Renter	.247
All	.594

A review of the voluntary market and MPIUA (FAIR Plan) portions of the overall 2003 loss ratio results (Exhibits 7 & 8) shows more favorable experience for the voluntary market than for the FAIR Plan. The 2003 loss ratios for the voluntary market and FAIR Plan are 57.5% and 83.9% respectively. The loss ratio for the FAIR Plan was

[18] Homeowners insurance loss ratios in the 60% or lower range are considered to be good underwriting results.

[19] Fire losses are an exception to this in so far as fires involving multiple dwellings can significantly impact losses for the year.

approximately 26.4% percentage points higher than the loss ratio for the voluntary market. This is not surprising or unexpected given the adverse selection and the current subsidies in the FAIR Plan rates. This FAIR Plan result along with prior year results show that the FAIR Plan's 1998 underwriting result (25.2% loss ratio) was a deviation from the norm.

A closer look at the loss ratios for the FAIR Plan large market share territories[20] (Exhibits 7 & 8) gives the following results

Massachusetts Homeowners Insurance Loss Ratios
Owners Forms

Territory	Territory Description	FAIR Plan Mkt. Share (2001-2003)	20 03 Vol. Market	FAIR Plan
2	Boston	42.9%	35.0%	47.8%
3	Boston	4.9%	173.1%	43.8%
4	Boston	66.8%	27.1%	78.0%
5	Suffolk except Boston	24.6%	37.5%	95.2%
11	Boston except 2,3 & 4	14.4%	38.6%	91.7%
30	Quincy	8.6%	45.2%	68.3%
32	Fall River	11.3%	50.5%	35.1%
33	New Bedford	18.0%	49.3%	52.9%
35	Brockton	18.6%	55.7%	92.8%
36	Plymouth except Brockton	7.2%	68.0%	120.4%
37	Barnstable, Dukes, & Nantucket	6.7%	65.3%	78.2%
38	Lawrence	35.3%	39.7%	105.8%
39	Lynn	19.4%	38.6%	41.9%
41	Cambridge/Somerville	6.2%	43.9%	86.8%
42	Lowell	10.8%	44.4%	98.7%
45	City of Worcester	10.2%	62.9%	80.1%
47	Springfield	8.4%	71.4%	102.9%
	Massachusetts	6.2%	59.1%	84.5%

These data generally show good voluntary market experience and poor FAIR Plan loss ratios for the majority of territories. FAIR Plan results have moderated somewhat across most territories falling between 2001 and 2002, loss ratio results which gave overall loss ratios for this form of 76.9% and 101.8% respectively. Exhibit 12 shows that total market water damage & freezing claims increased 72.9%. There was also an increase in Boston's 2003 annual snowfall, a proxy for Massachusetts snowfall, as shown in Exhibit

[20] Large market share territories are market share territories where the FAIR Plan market share equals or exceeds four percent (See Exhibit 1).

16, page 1. The voluntary market results shown above give mixed results with more territories higher and fewer territories lower than the 2002 results. However, the statewide voluntary loss ratio for 2003 is the highest for the 2000-03 period (59.1% vs. 54.9%, 57.1% and 48.9%). This also shows that the overall voluntary market results are generally more consistent from year to year than the FAIR Plan results (84.5% vs. 82.9% and 76.9% and 101.8%) over the same period. However, this is not surprising given that FAIR Plan loss ratio data is not as highly credible from a statistical standpoint.[21]

The number of FAIR Plan earned house-years by territory is such that the loss ratio experience can be expected to experience significant random fluctuations from year to year within individual territories. One example of this is territory 35 (Brockton). The voluntary market in 2003 had 16,502 total earned exposures that generated a total of 929 incurred claims. The FAIR Plan had 2,870 total earned exposures in the same territory that generated a total of 227 claims. It is not surprising in this territory that the FAIR Plan loss ratio dropped from 223.9% in 2002 to 91.7% in 2003 given this limited exposure and the resulting low credibility of the experience. Care should be exercised so as to not place too much weight upon any FAIR Plan individual territory loss ratio result for any one year when the loss ratio is based upon a relatively small number of house-years of insurance.

As expected a comparison of 2002 and 2003 loss ratio experience by territory reveals more variability in the FAIR Plan than the voluntary market.

Voluntary Market Loss Ratios-All Forms

Territory	2002	2003
2	64.3%	34.7%
3	119.8%	108.9%
4	130.7%	26.5%
5	43.5%	36.9%
11	35.8%	37.8%
12	28.1%	35.1%
30	52.7%	44.4%
31	53.7%	51.6%
32	33.8%	47.0%
33	43.0%	48.2%
34	41.0%	50.7%

FAIR Plan Loss Ratios-All Forms

Territory	2002	2003	Territory Description
2	60.1%	48.0%	Boston - District A
3	154.8%	41.5%	Boston - District B
4	136.0%	77.5%	Boston - District C
5	93.5%	94.4%	Suffolk (Except Boston)
11	93.1%	88.8%	Boston - Except Districts A, B & C
12	58.8%	7.5%	Brookline
30	62.4%	66.7%	Quincy
31	136.3%	111.7%	Norfolk (Except Brookline & Quincy)
32	142.2%	39.3%	Fall River
33	95.2%	54.5%	New Bedford
34	116.7%	56.1%	Bristol (Except Fall River & New Bedford)

Voluntary Market Loss Ratios-All Forms

Territory	2002	2003

FAIR Plan Loss Ratios-All Forms

Territory	2002	2003	Territory Description

[21] Exhibits 7 & 8 show the Voluntary Market with approximately 1.7 million written house years and 85,600 claims and the FAIR Plan with approximately 97,000 written house years and 4,700 claims.

35	45.7%	54.8%	35	223.9%	91.7%	Brockton
36	53.2%	67.2%	36	111.4%	119.7%	Plymouth (Except Brockton)
37	38.3%	64.7%	37	52.2%	78.2%	Barnstable, Dukes, and Nantucket
38	29.2%	38.9%	38	121.3%	106.4%	Lawrence
39	34.1%	38.6%	39	120.3%	43.6%	Lynn
40	44.3%	58.7%	40	113.7%	100.1%	Essex (Except Lawrence & Lynn)
41	34.6%	42.1%	41	25.1%	82.0%	Cambridge & Somerville
42	32.8%	44.2%	42	112.7%	98.0%	Lowell
43	60.2%	70.7%	43	38.2%	130.6%	Newton
44	45.6%	57.7%	44	94.3%	92.7%	Middlesex Remainder
45	51.6%	60.0%	45	84.6%	82.2%	City of Worcester
46	57.8%	60.8%	46	124.1%	108.4%	Worcester (Except City of Worcester)
47	42.1%	70.6%	47	105.2%	101.5%	Springfield
48	47.8%	66.3%	48	234.9%	21.0%	Chicopee & Holyoke
49	56.5%	63.8%	49	47.9%	108.2%	Hampshire & Remainder of Hampden
50	57.0%	70.3%	50	250.6%	86.1%	Berkshire & Franklin
Total	47.7%	57.5%	Total	100.3%	83.9%	Statewide

2003 Overall Cause of Loss Analysis

The overall causes of loss totals for the 2003 Massachusetts homeowners insurance market are shown at the end of Exhibit 10. The 2003 cause of loss claim counts as a percentage of total claims are similar to the 2002 cause of loss claim distribution except for fire*, lightning, and removal*, *wind and hail*, and w*ater damage and freezing*. *Water damage and freezing* claims in 2002 and 2003 as a percentage of total claim counts were 30.7% and 44.6% respectively. The change in these claim counts as a percentage of the total is surprising given the 2002 Boston snowfall was 24.5 inches versus 77.7 inches for 2003 (Exhibit 16, page 1). While the Boston snowfall is used as a proxy for the statewide snowfall, the correlation is not perfect. Other factors that impact this type of claim are the number of snowstorms and the corresponding number of freeze/melt cycles. Fire, lightning, and removal claims as a percentage of total homeowners insurance claims decreased from 13.4% in 2002 to 9.3% in 2003.

The other differences that occurred between the 2002 and the 2003 claims by cause of loss involve a decrease in the percentage of *wind and hail* claims from 13.7% in 2002 to 9.2% in 2003 and a decrease in the percentage of *theft* claims from 13.4% in 2002 to 10.3% in 2003. In 2002 there were two catastrophic events compared to one in 2003.

The catastrophic events[22] that impacted Massachusetts in both 2002 and 2003 involved *wind and hail* and w*ater damage and freezing.*

The *all other* cause of loss claims as a percentage of total claims decreased from 25.3% in 2002 to 23.8% in 2003. The *all other* cause of loss code is used when the claim doesn't fit one of the other causes of loss, when there is some question as to which cause of loss among several possible causes of loss caused the claim, or when the cause of loss is not known initially. In general, claims initially classified as *all other* are not subsequently reclassified.

The remaining causes of loss, l*iability and medpay,* shows a change in the percentage of total claims from 3.6% in 2002 to 2.8% in 2003. This is a change in the percentage of total claims of -0.8%.

A review of Exhibit 12 for the non-weather related causes of loss shows either relatively stable number of claims from year to year or small changes in the number of claims. The absolute number of claims for these non-weather related perils change in small amounts over time compared to the weather related causes of loss which show large swings in the absolute number of claims. This reinforces the susceptibility of homeowners insurance results to the fluctuations in the weather. The number of claims and amount of losses that are not weather related usually experience smaller changes from year to year in the absence of unusual happenings. The claims and losses related to the weather related causes of loss, *wind & hail* and *water damage & freezing*, will experience large changes due to severe or catastrophic weather events. The fact that non-weather related causes of loss don't experience large shifts in claims and losses from one year to the next is not the same thing as saying that non-weather related causes of loss claims and losses can't experience gradual shifts over time.

Cause of Loss Analysis by Territory[23]

Cause 1, F*ire, lightning and removal* losses decreased from 41.3% of total statewide losses in 2002 to 33.3% of total statewide losses in 2003. Territory 4 (Boston District C) fire losses still remained the highest in the state, even with a decrease, from 71.4% in 2002 to 62.9% in 2003. Other territories experiencing large decreases in fire losses in 2003 include Territory 12 (Brookline) which decreased from 38.4% in 2002 to 10.8% in 2003, Territory 39 (Lynn) which decreased from 54.4% in 2002 to 30.1% in 2003. Territories with high fire losses relative to the statewide percentage include Territory 3 (Boston District B) at 52.5% and Territory 38 (Lawrence) at 55.4%.

The statewide average fire claim cost was approximately $18,083 in 2002 versus $24,063 in 2003. The statewide number of fire claims decreased from 10,258 (13.4% of total) in 2002 to 8,514 (9.3% of total) in 2003. A closer look at the loss experience in Territory 4 (Exhibit 10) shows the number of fire claims in Boston District C decreased from 50 claims in 2002 to 27 claims in 2003. At the same time the average fire claim cost in

[22] Massachusetts catastrophe code numbers were assigned by Property Claims Services, Inc. (PCS), a subsidiary of ISO, Inc. This organization assigns catastrophe code numbers to natural events when insurable losses resulting from a natural event exceed $25 million and at least 2,000 claims.

[23] See Exhibit C for full territory description

Boston District C decreased from approximately $75,998 to $74,970. Territory 12 (Brookline) experienced an increase in fire claims from 16 in 2002 to 39 in 2003, however its average fire claim cost decreased from approximately $71,774 to $11,290 over the same period. Territory 39 (Lynn) experienced a decrease in fire claims from 73 in 2002 to 57 in 2003. The average fire claim cost for Territory 39 (Lynn) also decreased from approximately $34,054 to $23,880 over the same period. Territory 3 (Boston District B) experienced a decrease in fire claims from 20 in 2002 to 12 in 2003 with its average fire claim cost increased from approximately $97,721 to $226,754 over the same period. Territory 38 (Lawrence) experienced a decrease in fire claims from 69 in 2002 to 46 in 2003 with its average fire claim cost also increased from approximately $29,825 to $53,096 over the same period. It is clear that the 2003 statewide increase in the percentage of fire loss dollars was affected by both claim severity and claim frequency.

Cause 2, *wind & hail* losses decreased from 5.9% of total statewide losses in 2002 to 4.2% of total statewide losses in 2003. Territory 2 (Boston District A) experienced a decrease in wind losses from 5.6% of total homeowner losses in 2002 to 2.8% of total homeowner losses in 2003. Territory 44 (Middlesex Remainder) experienced a decrease in wind losses from 6.3% of total homeowner losses in 2002 to 3.7% of total homeowner losses in 2003. Territory 45 (Worcester City) experienced a decrease in wind losses from 7.2% of total homeowner losses in 2002 to 3.9% of total homeowner losses in 2003. Territory 46 (Worcester Remainder) experienced a decrease in wind losses from 7.9% of total homeowner losses in 2002 to 4.1% of total homeowner losses in 2003. Territories which experienced increases in percentage of total losses in this cause of loss include Territory 35 (Brockton) which went from 3.0% in 2002 to 4.5% in 2003 and Territory 48 (Chicopee & Holyoke) which went from 3.0% in 2002 to 6.6% in 2003.

The statewide average wind claim cost was approximately $2,531 in 2002 and $3,105 in 2003. Territory 44 (Middlesex Remainder) experienced the largest number of claims with a decrease in the number of wind claims from 1,797 in 2002 to 1,277 in 2003. At the same time its average wind claim cost increased from approximately $2,611 to $3,091.

Cause 3, *water damage & freezing* losses as a percentage of total homeowner losses increased from 22.2% in 2002 to 36.2% in 2003. The territories which experienced large increases in losses from this type of claim during this period included Territory 2 (Boston District A), Territory 35 (Brockton), Territory 37 (Barnstable, Dukes, Nantucket) and Territory 50 (Franklin & Berkshire). Territory 2 went from 8.0% of all losses in 2002 to 26.0% of all losses in 2003. Its claim count increased from 230 in 2002 to 450 in 2003, while its average claim cost increased from approximately $3,102 to $4,102 over the same period. Territory 35 went from 13.0% of all losses in 2002 to 34.0% of all losses in 2003. Its claim count increased from 256 in 2002 to 550 in 2003, while its average claim cost also increased from approximately $3,809 to $4,842 over the same period. Territory 37 went from 28.9% of all losses in 2002 to 50.8% of all losses in 2003. Its claim count increased from 1,641 in 2002 to 2,885 in 2003, while its average claim cost also increased from approximately $5,850 to $12,698 over the same period. Similarly, Territory 50 went from 13.2% of all losses in 2002 to 32.9% of all losses in 2003. Its claim count increased from 747 in 2002 to 1,983 in 2003, while its average claim cost also increased from approximately $3,185 to $3,875 over the same period.

Cause 4, *theft*, losses decreased from 4.6% of all losses in 2002 to 3.2% in 2003. The average statewide theft claim cost over the 2002-2003 period went from $2,030 to $2,118, an increase of 4.3%. The statewide number of claims decreased from 10,264 to 9,394. Territory 40 (Essex Remainder) saw a decrease in the number of claims from 952 in 2002 to 835 in 2003 or –12.3%. Territory 44 (Middlesex Remainder) saw a decrease in the number of claims from 1,543 in 2002 to 1,422 in 2003 or –8.5%. Territory 49 (Hampden & Hampshire Remainder) also saw a decrease in the number of claims from 794 in 2002 to 643 in 2003 or –19.0%. Territory 32 (Fall River), on the other hand, saw an increase in the number of claims from 110 in 2002 to 137 in 2003 or 24.5%. Territory 34 (Bristol Remainder) saw an increase in the number of claims from 597 in 2002 to 617 in 2003 or 3.4%. Territory 5 (Suffolk Remainder) also saw an increase in the number of claims from 153 in 2002 to 172 in 2003 or 12.4%. Most other territories experienced smaller increases or decreases in the number of claims from 2002 to 2003.

Cause 6, *liability & medical payments* losses as a percentage of total losses decreased from 11.2% in 2002 to 7.3% in 2003. The total statewide number of liability & medical payments claims decreased from 2,743 in 2002 to 2,518, or -8.2%. The corresponding statewide average claim cost decreased from $18,415 to $17,811, or -3.3% over the same period. Territory 3 (Boston District B) at 1.4%, Territory 5 (Suffolk Remainder) at 3.3%, and Territory 41 (Cambridge & Somerville) at 4.4% experienced larger decreases in liability and medical payment losses as a percentage of total losses. The Territory 3 decrease was primarily due to a 90.3% decrease ($38,627 to $3,736) in average claim cost as claim counts actually increased from 18 to 20 over the same period. The Territory 5 decrease was primarily due to a 47.3% decrease ($31,600 to $16,666) in average claim cost as claim counts decreased from 37 to 15 over the same period. The Territory 41 decrease was primarily due to a 69.8% decrease ($33,344 to $10,075) in average claim cost as claim counts increased from 43 to 47 over the same period.

Cause 9, *all other* losses increased as a percentage of total homeowners insurance losses from 14.7% in 2002 to 15.7% in 2003. The average statewide all other average claim cost increased from $3,413 in 2002 to $4,426 in 2003. The total number of all other claims increased from 19,397 (25.3% of total) in 2002 to 21,806 (23.8% of total). This cause of loss reflects losses where no cause is initially known, several causes may be involved, or a cause of loss that doesn't fall into one of the other causes of loss.

MPIUA Market Share and Rate Subsidies

The overall MPIUA market share based upon written premium has increased from 5.4% in calendar year 2001 to 7.1% in calendar year 2003. The MPIUA territorial market share by year based upon calendar year 2001-2003 written premium is shown in Exhibit 17. This exhibit shows relatively stable changes in MPIUA market share from 2001 to 2003. All of the MPIUA market share territories have increased this year from 0.3% to 9.3% with the exception of Territory 41 (Cambridge & Somerville) essentially remaining the same. Territory 5 (Suffolk Remainder), Territory 32 (Fall River), Territory 37 (Barnstable, Dukes, Nantucket) and Territory 38 (Lawrence) show some of the larger MPIUA market share increases of 3.2%, 3.9%, 3.2% and 9.3% respectively. The FAIR Plan dwelling forms policy counts for most non-Boston territories continue to increase in

raw numbers. Coastal territories as a percentage of FAIR Plan business appears to have increased both in percentage and raw numbers (as shown in Exhibit 19).

Exhibit 18 shows the annual number of homeowner's policies issued by the MPIUA from fiscal years 1994 through 2003. The overall increase in policies went from 50,466 in 1994 to 99,283 in 2003, an increase of 97.7%. Policies issued have increased over each annual period other than 1999 to 2000. The first large increase (15.3%) in MPIUA homeowners policies during this period occurred in fiscal year 1994. This fiscal year was the second fiscal year following Hurricane Andrew (1992) which caused such extensive damage in the southeastern United States. The 1994 increase was followed by annual increases in the number of MPIUA homeowners policies issued of 15.3% (1995), 9.4% (1996), 6.1% (1997), 2.7% (1998), and 4.1% in 1999. The 1.3% decrease from 1999 to 2000 (72,197 to 71,288) represented the first annual decline in policy counts in the 1994-2003 period. An increase of 4.7% occurred in 2001 and 12.8% in 2002. The 18.0% increase from 2002 to 2003 (84,157 to 99,283) represented the largest increase in the 1994-2003 period.

The large past increases in the number of MPIUA homeowners policies were dominated by the influx of coastal property policies into the MPIUA. This can be seen in Exhibit 19 detailing HO-2 & HO-3 (dwelling forms) policy counts by year by rating territory. Boston territories represented 26.3% of the MPIUA homeowners dwelling form policies as of December 31, 1997. The same Boston territories decreased to 17.5% of the MPIUA policies as of December 31, 2003. Coastal rating territories over the same period increased their share of these MPIUA policies from 22.8% to 25.8%. This represented an increase in the number of coastal territory policies from approximately 11,514 in 1997 to 21,377 in 2003, an increase of 85.7%[24]. Cape Cod & the Islands went from 4,559 policies in 1997 to 10,072 policies in 2003, an increase of 120.9%. Plymouth County excluding Brockton went from 5,403 policies in 1997 to 8,194 policies in 2003, an increase of 51.7%. Other areas that had large percentage increases in MPIUA policies over the 1997-2003 period include Territory 31 (Norfolk Remainder) 89.3%, Territory 32 (Fall River) 142.5%, Territory 35 (Brockton) 90.5%, Territory 39 (Lynn) 88.0%, Territory 45 (City of Worcester) 93.4%, Territory 46 (Worcester Remainder) 124.5%, Territory 47 (Springfield) 133.4%, Territory 48 (Chicopee & Holyoke) 213.6%, Territory 49 (Hampden & Hampshire Remainder) 241.4%, and Territory 50 (Franklin & Berkshire) 208.3%. The MPIUA statewide HO-2 & HO-3 counts increased 63.9% over the same interval. The MPIUA statewide HO-2 & HO-3 policy counts from December 31, 2003 to June 30, 2004 also increased from 83,011 to 96,170 up 15.9%.

A review of the MPIUA statutory profit or loss from Exhibit 18 shows a homeowners insurance underwriting profit of $7.7 million in fiscal year 1998[25] followed by an underwriting profit of $0.35 million in fiscal year 1999. This translates into an average underwriting profit per policy of $111 in fiscal year 1998 and underwriting profit per policy of $5 in fiscal year 1999, followed by an underwriting loss per policy of $26, $113, $84 and $138 in fiscal years 2000, 2001, 2002 and 2003. The average

[24] For purposes of this calculation territories 34, 36 & 37 are used.

[25] The MPIUA fiscal year runs from October 1st of the prior calendar year to September 30th of the current calendar year, e.g., fiscal year 2003 runs from October 1, 2002 to September 30, 2003.

underwriting profit/loss per policy over the fiscal year 1994-2003 period is a loss of $81 or $101 per policy if we exclude the unusual profit in the 1998 results.

In the 1994-2003 period these underwriting subsidies have ranged from a low of -$111 (surplus) per policy in 1998 to a high of $253 per policy in 1996. The MPIUA rate subsidies have been present in urban area rates for a number of years. Factors other than rate subsidies forced coastal insureds to seek coverage in the MPIUA after the voluntary market tightened for these types of risks. These factors included the unavailability of voluntary market insurance due to the cost of reinsurance and restrictions imposed on primary insurers by their reinsurers.

It is possible for rate subsidies in a residual or non-voluntary market to constrict the overall voluntary market. This can occur when the underwriting deficit for the residual market is of such a magnitude that it results in a high cost to be added to each voluntary policy so that the deficit subsidy amount added to each voluntary policy converts an otherwise profitable voluntary policy to a net loss policy. Massachusetts experienced this affect in its workers compensation and private passenger automobile markets prior to legislative reform[26] of these markets. The MPIUA deficit is not now, nor has it been, near that stage since its inception. The MPIUA deficits shown on Exhibit 18 should be measured against a Massachusetts voluntary homeowners insurance market of more than $1 billion in annual written premium.

A review of MPIUA rates relative to rates in the voluntary market (Exhibit 21) shows that MPIUA rates continue to be a bargain, especially in the large share territories[27]. The MPIUA rates are often among the lowest compared to the top ten insurers by market share[28]. The MPIUA rates appear to be even higher than they really are when the voluntary market underwriting criteria are factored into the comparison. These rates are low despite loss experience that would warrant a significant rate increase to bring rates to the break-even point, but for statutory prohibitions. Thus one of the impediments to reducing the FAIR Plan's market share in the large share territories is the fact that MPIUA rates are more affordable for identical coverage *offered* at higher prices in the voluntary market. This is supported by statistics from the MPIUA Market Assistance Plan (MA-MAP) in Exhibit 20. The most telling statistic in Exhibit 20 is the small number of insureds that even requested to be shopped around in the voluntary market, i.e., less than 100, when the MPIUA is writing approximately 99,283 homeowners policies. One would expect that if the issue of a voluntary market policy were the primary issue for FAIR Plan insureds, then a much higher number of them would check off the box on the FAIR Plan application so that the FAIR Plan would shop their homeowners insurance coverage in the voluntary market. It is clear that price is more important to these insureds, than the issue of which insurer provides coverage.

Coastal Property

[26] Chapters 398 and 399 of the Acts of 1991 and Chapter 273 of the Acts of 1988.
[27] This exhibit shows MPIUA rates effective as of 12/31/03.
[28] An insurer's lower rate for a certain classification of risk can be misinterpreted as competitive if the insurer's underwriting criteria result in relatively few offers of voluntary policies to risks in that classification.

Hurricane Andrew (1992) was a watershed event in property insurance. Its impact carried far beyond the southeastern United States that experienced the physical impact of this hurricane. Reinsurers increased general reinsurance rates and catastrophe covers following Andrew and the Northridge earthquake. Excess capacity in recent years and the passage of time following Andrew and Northridge had led to decreases in reinsurance costs from the high points following Andrew and Northridge. Prior to September 11, 2001 the reinsurance costs had started to increase once again due to poor underwriting results. The September 11, 2001 events created both a financial and psychological price and availability spike in the reinsurance markets. In 2003, revised catastrophe models, have fueled the increase in reinsurance prices. Many insurers have reported reinsurance price increases of 25% and higher for the same or even less coverage. Additionally, most reinsurers are excluding losses resulting from acts of terrorism. While the terrorism exclusion by reinsurers shouldn't have much direct impact on homeowners insurance, the reinsurance price increases, along with any writing restrictions, e.g., restrictions on coastal property or increased cost due to the level of coastal property, will have a direct impact. Some reinsurers limit their primary insurers' exposure to catastrophic loss by restricting the amount of coastal property in primary insurers' books of business they will reinsure. This resulted in more costal policies placed in the FAIR Plan.

The aftermath of Hurricane Andrew also saw the introduction of both wind deductibles and mandatory flood insurance requirements imposed by insurers. Many homeowners insurers require all insureds or insureds located in certain coastal territories, such as Territory 37 (Barnstable, Dukes, and Nantucket Counties), or insureds within 1,000 or 2,500 feet of the coast to have a minimum wind or hurricane deductible[29] on either a flat dollar or percentage of dwelling amount basis. It is most important in these situations that the consumer be given clear disclosure as to the coverage the consumer has in the event of wind or hurricane loss. This disclosure should be given to the consumer before the consumer has placed coverage with the insurer.

The MPIUA currently requires all insureds to have a minimum wind percentage deductible of 1% to 5% (of coverage A limit) or a minimum fixed dollar deductible from $0 to $5,000 depending on county, distance from the coast and coverage A limit.

Many homeowners insurers also require coastal insureds who may be susceptible to ocean storm surge to purchase federal flood insurance as an underwriting requirement for homeowners insurance coverage. In this situation the insured would have coverage and the insurer and the Federal Insurance Administration (FIA) could determine whether the homeowners insurance policy or the flood insurance policy were liable for coverage. In recent years the FIA has encouraged having one adjuster for both claims to help streamline the claims process for insureds. Insureds who have mortgages owned by the Federal National Mortgage Association (Fannie Mae) are required to purchase flood insurance if the property is located in areas susceptible to storm surge or floods.

The federal government is working through the Federal Emergency Management Administration (FEMA) to help assure that properties damaged in natural disasters are rebuilt/repaired to strengthen their ability to sustain, or avoid, the next similar disaster.

[29] A wind deductible is a deductible that applies only to losses caused by wind.

This means that homeowners policies will need to be able to provide coverage for the risk that rebuilding to the pre-loss condition or even at the pre-loss location might not be allowed. Changes (strengthening) in building codes are being encouraged by FEMA and the Massachusetts Emergency Management Administration (MEMA), (the state agency that works with FEMA on such matters). Both are also engaged in encouraging improvements in structures to help mitigate losses.

One of the problems related to ocean storm surge damage is the question of whether the loss was caused by wind that is a peril covered by the homeowners insurance or by ocean storm surge that is not covered by the homeowners insurance policy. In these cases if the insureds have not purchased federal flood insurance, then a wind claim is often filed with the homeowners insurer which places the insured and the insurer in the position that a denied claim means no recovery for the loss. If the insured has both homeowners and flood insurance, then the insured will have coverage whether the cause of loss is determined to be wind or ocean storm surge. Hurricane Isabel is a good example of this problem.

Prior to Hurricane Andrew, insurers used several decades of wind experience to determine an average excess wind factor to load into their rates. The purpose was to smooth out the effects of a catastrophic event such as a hurricane or tornado and prevented rate shock immediately following the catastrophic event. After Hurricane Andrew, insurers felt that the average excess wind methodology significantly understated the average wind load needed to compensate insurers for the potential catastrophic loss. This has led to the development of hurricane models in order to predict potential hurricane losses. These hurricane models are often proprietary computerized hurricane simulation models that combine multiple disciplines such as wind theory, meteorology, building engineering, historical enforcement of building codes, and financial theory. Hurricane models developed by a relative few modeling firms are used by the majority of homeowners insurers. These models have been refined and recalibrated in recent years.

Cancellation & Non-Renewal Data

The top twenty-five homeowners insurers[30] by Massachusetts market share were required[31] under Chapter 175, §4B to file a listing of policies in force, cancellations, and non-renewals by zip codes designated by the Commissioner on a calendar year basis for policies written on or after January 1, 1994. In addition insurers are requested to provide the number of cancellations and non-renewals initiated by the insurer and insurer initiated non-renewals because of claim frequency.

This year (as with last year's report) any questionable individual company data was again run by the companies to verify that the data they submitted to the Commissioner was in fact their correct data.

[30] Exhibit 22 provides a list of insurers and each of their individual insurance companies that were writing homeowners insurance in Massachusetts in 2003. Some of these insurers are better known by the names of their individual insurance companies.

[31] Cancellation and non-renewal data is not currently captured by any of the homeowners statistical plans.

This year's submissions included such data for calendar year 2003. This requirement is detailed in Exhibit 2. The cancellation & non-renewal listings, unlike company specific premium and loss data, are to be considered public records under this statute. The individual insurer listings and the MPIUA listing are detailed in Appendix A. The industry aggregate (top twenty-five insurers) listing of cancellations and non-renewals by designated zip codes is shown in Appendix B.

This year's report includes for the fifth time a summary comparison of urban and coastal writings by insurer (see Exhibit 23). This exhibit compares the number of individual insurer 2003 urban and coastal policies-in-force in the selected zip codes relative to each percent of statewide voluntary market share. This is one way to make an equitable insurer by insurer comparison of the number of urban and coastal writings in the selected zip code areas.

Exhibit 23 shows that only a couple insurers ranked near the top in writing policies in both urban and coastal zip code areas by percent of voluntary market share. They are Providence Group (7^{th} & 3^{rd}) and Vermont Mutual Group (2nd & 7^{th}) in urban and coastal areas respectively. Other insurers ranked near the top in one of the two categories. In the urban category Royal & Sun Alliance USA (1^{st}), Preferred Mutual Insurance Company (3^{rd}) and Union Mut-VT (4^{th}), represented some of the top urban writers by policies by percent of voluntary market share. In the coastal category Hingham Mutual Group (1^{st}), White Mountains Group (formerly OneBeacon Insurance Group) (2^{nd}), National Grange Mutual Insurance Group (4^{th}) ranked near the top. However, urban and coastal property continues to be a problem for some insurers. Chubb & Son, Inc. (25^{th}), Allianz Group (24^{th}), and USAA Group (23^{rd}) had the lowest number of 2003 urban policies-in-force per percent of voluntary market share. Commerce Group, Inc. (25^{th}), Royal & Sun Alliance (24^{th}), and Preferred Mutual (23^{rd}) had the lowest number of 2003 coastal policies-in-force per voluntary market share.

One insurer, CNA Insurance Group, was added and one insurer, Pawtucket Mutual Group, was deleted from the top twenty-five homeowners insurer list.

Insurer percentage for voluntary market share ranges from –0.8% to +0.9%. Some of the insurers that had the largest voluntary market share increases were Commerce Group, Inc. Chubb & Son, Inc. and Quincy Mutual Group at +0.9%, +0.5% and +0.5% respectively. White Mountains Group, Harleysville Group, Norfolk & Dedham Group and Allmerica Financial Group showed the greatest voluntary market share decreases at -0.8%, -0.4%, -0.2% and -0.2% respectively.

Also, this year's report includes for the second time, an exhibit that shows insurer initiated urban and coastal non-renewals as a percentage of urban & coastal policies in force (see Exhibit 24). This is one more way to make comparisons between insurers.

Exhibit 24 shows the insurers that have the lowest percentage of insurer initiated non-renewals of urban & coastal policies in force are Harleysville Group (0.00%), Arbella Insurance Group (+0.04%) and CNA Insurance Group (+0.06%). The insurers that are

highest are Plymouth Rock Insurance Group (+13.62%), White Mountains Group (+11.24%) and Norfolk & Dedham Group (+6.67%).

If an insurer's rates are higher than the FAIR Plan premium rates in a particular urban or coastal rating territory, then the insurer may not get business in that territory because its rates are not competitive with the FAIR Plan. A review of Exhibit 21 shows that a number of the top ten insurer rates in urban areas are higher than those offered by the FAIR Plan. Thus in those territories those insurers' rates are a disincentive for a potential insured to select a voluntary policy of the same type as offered by the FAIR Plan. If an insurer has no agents or production offices in urban or coastal areas, then it usually follows that they would have few or no policies in the same areas. By all reports, internet sales remain well behind independent agents and production offices in generating business. Internet sales have had little impact in the Massachusetts homeowners market which doesn't have participation from the top three or four countrywide personal lines direct marketers. If an insurer markets to a specific market segment or niche and that market segment or niche is not present in urban or coastal areas, then that insurer may have little or no writings in those areas. Insurers' contracts with their agents and brokers often provide for additional compensation for business that produces desirable loss levels. In addition, some contracts require certain levels of production in order for certain products to be made available for sale. All of the above must be factored into consideration when analyzing why insurers write business in certain areas and not in others.

Premium & Loss Experience by Designated Zip Code

Again this year, Chapter 175, § 4A required statistical agents for Massachusetts homeowners insurance to submit premium and loss experience by designated zip code for the top twenty-five Massachusetts homeowners insurers by written premium and the MPIUA. The statute explicitly categorizes the individual insurer data as confidential and not to be made public except under well defined conditions. The Division has produced a 2003 aggregate premium and loss experience report for the top twenty-five insurers and the MPIUA for the designated zip codes as shown in Appendix C.

Care should be exercised in drawing conclusions from one year's loss experience for a particular zip code. This data for most individual zip codes may not be 100% statistically credible. This means that one can expect significant random variation in the individual zip code loss experience from year to year. For example, the loss ratio for a particular zip code could be a favorable 25% in one year and an unfavorable 175% the next year. Additionally, calendar year 2003, as previously discussed, is generally considered to have been a good year for Massachusetts homeowners insurance experience. Focusing on the individual year experience from a good or bad year will not provide correct inferences regarding the underlying loss potential for an individual zip code. That being said, the overall total market loss ratio experience for the designated zip codes is 58.5%**.** This loss ratio result is approximately 11.3% higher than the 2002 loss ratio result of 47.2% for similar zip code areas. The 58.5% is considered a very good underwriting result.

New & Emerging Issues in Homeowners Insurance

Acts of Terrorism

The events of September 11, 2001 and the resulting response of reinsurers toward their reinsurance coverage has brought the issue of terrorism exclusions to the forefront. The main area of concern for insurable property & casualty losses resulting from acts of terrorism lies with commercial lines of insurance. However, there is an indirect impact on homeowners insurance cost and availability as a result of the September 11, 2001 events; namely, the cost of reinsurance & the lack of insurance availability.

President George W. Bush signed the Terrorism Risk Insurance Act of 2002 on November 26, 2002. The Act provides a federal back-stop for claims arising from some terrorism events and requires that coverage for certain terrorism events be offered to commercial policyholders. However, the Terrorism Risk Insurance Act of 2002 does not apply to any personal lines insurance policies, including homeowner policies. The Massachusetts Division of Insurance continues to prohibit the attachment of any terrorism exclusions to homeowner policies.

Reinsurance Costs & Restrictions

Many primary[32] insurers have reported significant increases of 25% or more in reinsurance costs for 2003. This means that primary insurers generally have a higher overhead in 2003 than they had in 2002. It is expected that insurers will pass this increase in cost on to their customers through higher rates. In some cases reinsurers may decline to renew policies with primary insurers because of certain lines of insurance or books of insurance written by the primary insurer. The amount of coastal property a primary insurer writes is one factor that reinsurers consider in pricing reinsurance for that primary insurer. It is also a factor that reinsurers consider in deciding whether to even offer coverage to the primary insurer.

Toxic Mold

One of the recently emerging issues in homeowners insurance across the country has been the issue of toxic mold property, personal injury & liability losses resulting from water damage. This issue received nationwide attention with the Ballard case in Texas. In June 2000 a Texas jury awarded Melinda Ballard and her family approximately $33 million (including $12 million in punitive damages) in their case against their homeowners insurer, Farmers Insurance.[33]

While Texas and California have seen the greatest increases in toxic mold claims[34], there have been other significant increases in such claims in the Southeastern U.S., Northwestern U.S., and even the Midwestern U.S. In addition to using frequency of toxic mold claims, the homeowners market is also facing increased severity of individual claims.

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[32] Primary insurers are insurers selling insurance to consumers, either personal or commercial. Reinsurers are insurers selling insurance to primary insurance companies in order to spread the risk of the primary insurer.

[33] The Ballard toxic mold case ($33m award) was significantly reduced on appeal to $4 million plus interest.

[34] Homeowners policies in Texas generally covered losses from "accidental water discharges" versus the standard "sudden and accidental discharges".

In general, the Northeast and Massachusetts in particular has seen little or no significant increase in toxic mold claims during calendar year 2003. Nevertheless, the national trend to limit or mitigate the losses associated with mold, toxic or otherwise, has reached Massachusetts.

Currently, the Division is prohibiting insurers from completely excluding coverage for toxic mold. The Insurance Services Office, Inc. (ISO) the largest rating organization in Massachusetts homeowners insurance filed with the Division on November 27, 2001 mold (i.e., *Limited Fungi, Wet or Dry Rot, Or Bacteria Coverage* Endorsement) limitation endorsements, rules, and loss costs for homeowners, dwelling fire, and personal liability insurance. The basic option includes first party (property) coverage of $10,000 and third party (liability) coverage of $50,000, both at no additional cost. The first party coverage has optional limits of $25,000 and $50,000 at loss costs of $27 and $46 respectively. The third party coverage has an optional limit of $100,000 at a loss cost of $4. On December 12, 2001 these endorsements were approved by the Division to be effective May 1, 2002. Consistent with ISO's approved endorsements, the Division is requiring all insurers to provide base coverage in the amount of $10,000 for first party property coverage and $50,000 for third party liability coverage. In addition, the Division is requiring all insurers to offer to the homeowner the option of purchasing additional coverages in the amounts of $25,000 and $50,000 for first party property coverage and $100,000 for third party liability coverage.

Introduction of the ISO HO 2000 Program

The ISO Homeowners Program is the leading Massachusetts homeowners insurance program used by the majority of insurers in Massachusetts.[35] It is considered the standard program against which all other programs are measured. On December 1, 2000, ISO filed its revised homeowners program, the so called *HO 2000 Program*. This filing generally a broadened the coverage provided by the HO 91 Program (see below) and was ISO's first comprehensive revision of its standard homeowners insurance program since the HO 91 Program approved in Massachusetts back in 1991. On March 19, 2001 the *HO 2000 Program* was approved by the Division to be effective as of September 1, 2001.

The revisions and additions included in the new standard program can be generally categorized as policy form changes, revised endorsements, and new endorsements. The following items are examples of how the *HO 2000 Program* expands upon the *HO 91 Program.*

New Forms

1. Introduction of HO-5 (Open Perils Coverage on Buildings & Contents, Excludes Earth Movement Coverage on Contents)

Form Revisions

1 Increased Limits of Liability Under Coverage C-Personal Property Special Limits of Liability

2. Increased Limits of Liability Under Coverage C-Personal Property-Business & Electronic Apparatus

[35] Most insurers market the basic ISO Program with a few minor modifications.

3. Increased Section I Limit of Coverage on Debris Removal
4. Additional Section I Coverage-Grave Markers On or Away from Residence
5. Broadened Section II Coverage for Owned Motorized Golf Carts
6. Increased Section II Damage to Property of Others Limit

New Endorsements

1. Other Members of Your Household Endorsement (Accommodates Insureds with Non-Traditional Households)
2. Assisted Living Care Coverage Endorsement (Provides Limited Coverage for Personal Property & Liability for Relatives Declared on the Schedule of The Endorsement)
3. Replacement Cost Loss Settlement for Certain Non-Building Structures Endorsement (e.g., Walls, Decks, Patios, Walks, etc.)
4. Scheduled Personal Property Endorsement (with Agreed Value Loss Settlement)
5. Owned Motorized Golf Cart-Physical Loss Coverage Endorsement
6. Residence Held in Trust Endorsement (Trusts Will Now Be Eligible for the Homeowners Program)

Recommendations

Previous Recommendations that Remain Valid

It has been eight years since the first Report on the Current State of the Homeowners Insurance Market in the Commonwealth was produced. Consumers continue to express the belief that rejections are based on illegal discrimination for no other reason than the failure of insurers to provide specific reasons for rejection[36]. Providing consumers with specifics that they might be able to address and thereby improve their ability to be insured in the voluntary market could well result in a general improvement of the market as a whole. Since MPIUA losses are ultimately shared by everyone who purchases the coverage, including those in the voluntary market, savings could be realized over time as properties are upgraded based on recommendations.

1. Insurer Underwriting Guidelines

It would be helpful to an insured if s/he had knowledge of individual insurers homeowners insurance general underwriting practices. The insured could then determine which insurance companies would probably write their specific property, saving time and money for the consumers and the industry. For example, if a consumer has a wood burning stove, then it would save the consumer time and effort if s/he knew which carriers would insure risks with wood burning stoves. The Division of Insurance currently has no statutory authority to require insurers to file their basic underwriting guidelines with the Division, but would welcome the opportunity to make these available for public inspection if insurers submitted them.

[36] Insurers often refer to "underwriting guidelines or standards" as the basis for rejection.

Appendix D includes existing regulatory language from New Jersey and Arizona. This is being provided to stimulate discussion and to show that such requirements exist elsewhere in the United States.

2. Declination of Coverage, Non-Renewal, Cancellation

It would be helpful if insureds were given useful information relative to their property in situations involving insurer declination of coverage, non-renewal, or cancellation. Citing "underwriting standards" is not specific enough to be useful. Specific physical deficiencies such as a badly worn roof, rotted clapboards, storage of old paint cans representing a fire hazard, aggressive dog or breed, etc., would allow consumers to consider correcting the deficiencies which prevent their purchase of homeowners coverage. It would also help prevent losses and the personal tragedies that too often accompany them. One could expect to see increased safety for occupants and firefighters, additional safety for abutters, and improvement in the housing stock as policyholders made changes to improve the insurability of their property. Again, Appendix D is supplied to assist consideration of this recommendation.

3. Coverage for Insureds Who Complete A Homeowner's Risk Management Course

Currently, a number of insurers provide discounts off homeowners insurance premiums to insureds who successfully complete a homeowner's risk management course conducted by the Massachusetts Affordable Housing Alliance (MAHA). This course educates consumers in steps they can take to maintain their property and prevent or minimize potential homeowners insurance losses. More such courses can be established and insurers should be encouraged to write and offer premium discounts to potential insureds that have successfully completed such courses.

While the original idea was to help people in territories where the voluntary market was not strong, the idea could well be expanded to the entire Commonwealth.

Appendix E lists the insurers currently offering premium discounts for the MAHA course completion.

4. Declination of Coverage, Non-Renewal

News stories highlighting the issue of insurer initiated non-renewals, in the face of a homeowner incurring one or more homeowners insurance losses, have been somewhat misleading. Insurance is a pooling mechanism whereby many insureds pay relative small amounts to fund the larger losses of a relative few. Insurers expect an insured to have homeowners insurance claims periodically over a multi-year period, but the occurrence of two or more claims in a relatively short time frame may concern an insurer. If an insured has three or four claims within a couple of years, then these claims may go to the standard of care that the particular insured is exercising in relation to the care of their

property and the resulting liability[37]. No insurer wants to write an insured that has shown a lack of care for their property.

On the other hand, these situations need to be examined on a case by case basis. Is the filing of two or three claims evidence of a lack of reasonable care of property or are these claims the result of chance events? For example, if an insured has a water damage & freezing claim one year and a theft claim the following year are these claims necessarily a lack of reasonable care? They may or may not be depending upon the individual circumstances involved. Insurers can non-renew an insured based solely upon the filing of a few claims in a two or three-year period, whether or not the insured had any responsibility for the losses. If there is an increased physical hazard, then the homeowner should be made aware by the insurer of the specific nature of any problems. As previously stated, insurer references to "underwriting reasons" provide little information that is helpful to the homeowner in terms of correcting any physical or behavioral deficiencies.

5. The data collection system in Exhibit 2 (M.G.L. c. 175, §4B) does not differentiate between cancellations and non-renewals generated by insurers and those generated by insureds. Clearly the statistics that provide the most relevant information in terms of redlining or aqualining[38] are those where the insurer initiated the cancellation or non-renewal. Traditionally, the majority of the top twenty-five insurers have voluntarily provided this information with the exception of the data requested for the first time last year for the number of non-renewals initiated by the insurer because of claim frequency. Two insurers failed to report the data[39]. A couple of inurers noted that they are creating a system or would be improving their current system for such future data requests. I recommend the statute be amended to require each insurer to provide statistics on insurer initiated cancellations and insurer initiated non-renewals in the future.

[37] Beginning in with the 2002 calendar year, insurers were requested to report the number of non-renewals that were initiated by the insurer because of claim frequency.

[38] Aqualining refers to unfair discrimination in the writing of coastal property merely because the property is on or near the coast. (In cities like Boston, there is the possibility that one person may believe a rejection is caused by "redlining" while another may believe the rejection is caused by "aqualining", since neither term has a universally agreed to definition.)

[39] Arbella Insurance Group and National Grange Mutual Insurance Group failed to provide data for non-renewals initiated by the insurer because of claim frequency.